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UNCLAS SECTION 01 OF 02 LILONGWE 000688

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SUBJECT: MALAWI RE-EXAMINES ELECTRICITY CONNECTION WITH  
MOZAMBIQUE

LILONGWE 00000688 001.2 OF 002

#### Summary

1. (SBU) Malawi's Parliament deferred approval of a proposed connection of the national electrical grid to the Southern African Power Pool (SAPP). An already approved World Bank loan to finance the infrastructure is due to expire on December 31, 2009. Lack of reliable electrical power has been identified as a major constraint to development in Malawi, where installed capacity is already below peak demand. The proposed interconnector would improve access and reliability and provide Malawi's hydro-dependent system with insurance against drought. The interconnector project, however, is complex and involves multiple agreements and uncertain costs. Until now the project has received little scrutiny and it has been poorly explained to the public and parliament. While committee hearings clarified many issues, the review occurred days before the World Bank deadline. The GOM has requested an extension of the deadline, which World Bank officials told us has a 50/50 chance of approval. It appears likely that Parliament will pass the bill when it returns in January, but it is not certain that the President will sign it. End summary.

#### Interconnector Bill Referred to Committee

2. (U) On December 4, Parliament referred to committee a bill to approve construction of an electricity connection between Malawi and Mozambique. Brought to the floor unexpectedly by Minister of Finance Ken Kandodo, the bill received broad support for the principle of the connection, but serious concerns about costs led to its referral to committee. It is now anticipated that the bill will be reintroduced for a vote during the Parliament's next sitting to begin in January.

3. (SBU) The interconnector project includes World Bank credit financing, approved in 2007. The Bank has twice extended the time to access the credit, with the current deadline falling on December 31, 2009. The GOM has requested a further extension of the deadline until the next sitting of the Parliament, but World Bank officials told us on December 21 that the chance for approval of the extension is only 50/50.

4. (U) Parliament's Budget and Finance Committee held hearings on the bill in early December, meeting with representatives from the relevant ministries, the Electricity Supply Company of Malawi (ESCOM), Malawi's Millennium Challenge Account team, and civil society. Reports from the hearings indicate it is likely the committee will recommend approval of the bill.

## Why an Interconnector?

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15. (U) Malawi's electrical grid is entirely self-contained, with no links to foreign power sources. The system currently has an installed generation capacity roughly 27 megawatts below its peak demand. This leaves no margin for equipment to be taken off-line for maintenance or repair. Load-shedding is an every-day occurrence. With a national access rate of only 7 percent, Malawi has one of the lowest levels of electrification in the world. Lack of access to reliable power has been identified as a major constraint to Malawi's economic development. With no new capacity expected to come on line until 2015, a connection to the Southern Africa Power Pool (SAPP) would allow Malawi to buy electricity to meet increasing demand and to fill gaps when generation equipment is being serviced. It would also enable Malawi to sell power to other countries during off-peak hours or if additional generation capacity is developed.

16. (U) Malawi's current unreliable power situation discourages new investment. It also costs current Malawian businesses that are forced to compensate for unreliable power with back-up diesel generators. At current oil prices the cost of diesel generation is nearly four times the estimated cost of power through an interconnector, with the demand for fuel involved contributing to already severe pressures on Malawi's available foreign exchange.

17. (U) With 98 percent of Malawi's electricity generated from hydropower facilities on the Shire River, the interconnection with the SAPP would also serve as insurance against drought. From 1994 to 2002 the water flow in the river was 50 percent below long term averages, and from 1917 to 1935 the Shire

LILONGWE 00000688 002.2 OF 002

stopped flowing entirely.

## A Complex Project, With Unknown Costs

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18. (U) The interconnector project includes three agreements: separate World Bank loans to Malawi (USD 48 million) and Mozambique (USD 45 million) to finance construction of the infrastructure, and a bilateral agreement between electrical utilities in the two countries. All of the agreements relate to the infrastructure only. There is currently no power purchase agreement, and any power that Malawi imports would need to be negotiated separately.

19. (U) One provision of the bilateral agreement that raised concern is the requirement that Malawi pay roughly USD 529,000 per month in fees to Mozambique. According to the World Bank, these "wheeling charges" (electricity carrying charges), constitute cost-recovery for Mozambique's share of the infrastructure investment. While renegotiation of the agreement is possible if both parties agree, the Malawians current concern is that the "wheeling charges," if paid for the length of the 20-year agreement, would far exceed Mozambique's loan obligation.

110. (U) We expect these charges would be nearly canceled out by fees charged to Mozambique once a projected extension of the line to northern Mozambique is completed. This extension, however, has not yet been formally negotiated, nor has the level of any such "reverse wheeling charges." Furthermore, even if the extension proceeds with no problems, there is likely to be a two- to three-year gap after the first phase is complete during which Malawi would need to pay charges before it can collect any from Mozambique.

111. (SBU) World Bank officials told that the GOM specifically chose not to include a power purchase agreement in the project. The lack of an agreement generates more cost uncertainty because Malawi would pay spot prices that are

subject to unpredictable fluctuations or increases and it would be vulnerable to uncertain power availability. If power from Mozambique's Cahora Bassa facility (the natural first option) is fully committed to other customers at the time, Malawi would need to buy from elsewhere in the pool, potentially two or three countries away, increasing wheeling charges substantially.

Comment

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¶12. (SBU) Up against the World Bank deadline, Parliament and the Malawian public have raised serious questions over the Malawi-Mozambique interconnector. We believe these concerns are manageable, either with better explanation or some further negotiation of the bilateral agreement. Malawi's power issues demand urgent attention, and the link with the Southern Africa Power Pool is the best alternative. While it appears possible that the World Bank will approve the extension, and likely Parliament will approve the project, the President's support remains far less certain.

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